

## AMERICAN TRADE POLICY AND THE TRADE BALANCE

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**U.S. Trade Deficit Review Commission  
Washington, D.C.**

**February 24, 2000**

Russell Baker of the New York *Times* used to say that Americans will “do anything for Latin America but read about it or think about it.” I imagine he would modify this somewhat if asked about trade deficits: Americans read about them, but rarely think about them and what they mean.

I applaud the Commission’s work. By making us think about the trade deficit, the results of your hearings and research can be immensely valuable as the public and Congress debate American trade policy in the years ahead.

### U.S. TRADE RECORD AND PHILOSOPHY

I will open by making a few points about the general philosophy of American trade policy, and then discuss the interplay of trade policy and the trade deficit.

U.S. trade policy generally has not set the goal of achieving particular levels of trade balance. To begin with, as previous Administration witnesses before the Committee have noted, overall balance levels are mainly the result of macroeconomic factors. For example, the robust growth in the United States in the past two years, in contrast to weak growth and recessions abroad, have helped to increase the trade deficit.

Our view, therefore, is that U.S. trade policy should be measured by its success in achieving goals such as removing foreign barriers to our exports; and by **fundamental** results such as expanding exports and the high paying jobs they support, raising real purchasing power and living standards for Americans, and encouraging long term growth. This has been the guiding principle of American trade policy since the New Deal under the Administration of Franklin Roosevelt.

### CLINTON ADMINISTRATION RECORD

Since then, Administrations of both parties have designed trade policy less to achieve particular levels of import-export balance than to contribute to larger economic goals of rising living standards and long-term growth. And the Clinton Administration’s trade policies have been squarely in this tradition.

Building upon a bipartisan record of achievement, for which Ambassador Hills among others deserves a great deal of credit, we have completed nearly 300 separate trade agreements. These include three which have **fundamentally** changed our country's trade environment, both through further opening our own economy and through greatly increasing the opportunities available to us in foreign markets.

First, we cemented our most important relationships – those with our immediate neighbors, Canada and Mexico, which make up more than one dollar in three of all our trade with the world – through passage of the North American Free Trade Agreement in 1993.

Second, we strengthened the rule of law and opened markets worldwide through the completion of the Uruguay Round Agreements and creation of the WTO in 1995. Together with this we have pursued numerous bilateral market-opening agreements with Japan, Europe, Canada, Latin America and Korea. Our agreement on China's WTO accession is a similar step forward, opening the markets of the world's most populous nation to a degree unprecedented in the modern era.

Third, after the creation of the WTO, we completed a set of agreements on information technology products, telecommunications, financial services and most recently electronic commerce, that open the world to the high-tech products and services in which our country excels.

Thus, trade policy – together with a strengthening commitment to education and job training, investments in science and technology at home, and a restoration of fiscal discipline – has helped to fundamentally improve our country's situation.

Ninety-three years ago, Winston Churchill proclaimed that:

“the country in which the superfine processes are performed – the superfine [being], the most complicated terminal stages of manufacture – is the country which possesses that which [is] called commercial ‘leadership.’”

Over the past decade, America has indeed built a record of commercial leadership:

- **Growth** Economy has expanded 3 1% to \$9.2 trillion in real terms, during the longest economic expansion in America's history. The expansion of exports during this period, totaling well over \$300 billion, accounted for a third of our growth until the recent financial crisis. Especially impressive has been the growth in American manufacturing, with production rising from \$1 trillion to \$1.4 trillion during this period.
- **Job Creation**: Our economy has created over 20 million new jobs, including a net gain of 259,000 manufacturing jobs.

Interesting to note: net job creation in Germany and Japan, whom we once held up as the paragons of excellence, rose by a paltry 130,000 jobs over the same period. Both are trade surplus countries (as is Russia, incidentally. My staff informed me this morning that Russia's surplus on goods trade is \$32 billion – the third largest of any country). In contrast to Japan and Germany, our unemployment rates have fallen from 7.3% to 4.0%. This is the lowest unemployment rate since January of 1970. These benefits have been shared widely throughout our economy, with African-American and Hispanic unemployment rates the lowest ever measured. Nearly 12 million American jobs are related to exports.

- Technological Progress: Our economy is more competitive, with unprecedented technological advance and rising rates of investment. Impartial observers have rated us the world's most competitive economy for the past seven years.
- Increased Investor Confidence: Our competitive superiority has attracted massive capital flows into the U.S. The United States' share of world foreign direct investment has sharply increased, with foreign countries investment rising from \$45 billion in 1994 to \$193 billion in 1998 (Germany, I am told, has invested more in the U.S.A. in the last three years than in Europe). Many had expressed fears that a more open world would promote investment in countries with lower wages or weaker labor and environmental standards. Investment decisions obviously have many causes, but experience shows that our high standards have not been a deterrent to investment in the United States.
- Rising Living Standards: Our families enjoy higher living standards, with average wages for non-supervisory workers reversing a twenty-year decline to grow by 6.8% in real terms since 1992; record rates of home ownership; sharp declines in the poverty rate; and unprecedented growth of family assets, investment in mutual funds, and other measures of financial well-being. Over 80 million Americans are now invested in equities. This is a dramatic statement of the evolution of our society: any astute politician will notice that as many people read the green (Money) section of *USA Today* as do the red (Sports) section, The American dream used to be owning a home; now it is to also own a well-performing mutual fund.
- Economic Security: While trade is **often** considered a factor promoting change, trade policy has also helped to give us guarantees of economic security in crisis. This was made very clear during the Asian financial crisis, when our network of trade agreements helped to prevent a worldwide cycle of protection and retaliation that would have done immense damage to American farmers, manufacturing exporters and our overall economic health.

Finally, a comment that is particularly relevant to my generation. I mentioned that our unemployment rate has fallen to its lowest level since 1970, when we last had 4% unemployment. In 1970, trade as a fraction of GDP – the sum of exports and imports of goods and services – was 13%. Today it is 3 1%. Then, at the height of the hot war in Vietnam and the Cold War with the

Soviet Union, defense spending accounted for 8% of GDP. Today it accounts for 3%. We have accomplished since 1970 a shift from creating employment and structuring our economy through conducting and preparing for war to an economy driven by the more **peaceful** challenge of competing internationally on the economic front.

## THE **TRADE** DEFICIT

Based on these most fundamental criteria, therefore, trade policy should be judged a success. The record of the past seven years, however, has also coincided with a sharp increase in our trade imbalance, **from** a rough balance during the last recession in 1991, to a deficit (goods and services) of about 1.4% of GDP in the period between 1994-1997 (compared to 3.2% of GDP in the late 1980s); and then to last year's level of \$271 billion, or 2.9% of GDP.

Administration officials appearing in previous meetings of the Trade Deficit Review Commission, notably Dr. Robert Lawrence of the Council of Economic Advisors, have ably laid out the reasons for this increasing deficit. As Dr. Lawrence noted, the growth of the deficit has been driven by many factors, most notably:

- The strong growth of the U.S. economy coupled with weaker economies abroad. This reflects the recent financial crisis, which cut U.S. exports to South Korea, the **ASEAN** states and much of South America; the recession in Japan, leading to a decline of approximately \$8 billion in exports; and a period of slower growth in Europe. Thus, while imports have continued to grow at rates comparable to those of the **mid-1990s**, exports remained at levels between \$917 billion and \$932 billion from 1996 to 1998, and have only recently begun to grow again.
- Stronger U.S. national investment, given that investment rates have risen more rapidly than national savings rates (since 1991 national investment rates have grown by 4.4% points while national savings rate are up by 2.5% points).

The difference in growth between the U.S. and the rest of the world has led to an increase in our trade deficits with almost all of our major trading partners:

Goods Trade Deficit (\$Billions)*			
<u>Country/ Region</u>	<u>1997</u>	<u>1999*</u>	<u>Change</u>
Japan	56.1 billion	73.9 billion	17.8 billion
China	49.7	68.7	19.0
Other Asia	15.8	44.1	28.3
EU-15	16.8	43.7	26.9
NAFTA	30.0	54.9	24.9
Latin America (excluding Mexico)	9.3 surplus	3.2	12.5

\*Final 1999 service export figures by country will not be available for several months. The U.S. typically runs a substantial services trade surplus; the figures above thus represent only goods trade and overstate the total goods and services trade imbalance.

Looking ahead, it appears likely that strong growth in the U.S. market will keep imports growing. This is not a cause for regret; as noted earlier, imports tend to promote competition, raise living standards and keep inflation low. Go to any store where ordinary Americans shop – Target or Home Depot or, in the rural areas of East Texas, Dollar General, and you will see the shelves stocked with imported goods that help our consumers stretch their hard-earned dollars and cut the cost of living.

U.S. exports of goods and services appear to be resuming their earlier rapid growth as prospects for the world economy are beginning to brighten, and global growth accelerates. Exports of American goods and services have risen from year earlier levels for the last 8 months (through December 1999) with an average monthly gain of 3.7%, whereas in 11 out of the preceding 12 months (May 1998 to April 1999) they had fallen.

### **TRADE POLICY AND FUTURE TRADE BALANCE LEVELS**

As this analysis and statistical review indicates, trade policy is likely to have only a small effect on overall U.S. trade balance levels.

Conceptually, a return to substantially higher trade barriers, would kill two birds with one stone: protectionism would be very damaging to America's poor and would likely prompt retaliation against American farmers and manufacturing workers, while having at most a minimal effect on U.S. deficit levels. In fact, by threatening foreign economies and reducing demand overseas, it would simply shrink both exports and imports, and would be likely to force American workers to move from higher-wage, higher-skill fields to less rewarding jobs.

A further program of market-opening – as we have laid out in our negotiating agenda at the WTO, with our major bilateral trading partners, and with respect to China's WTO accession – will allow us to build upon the successes we have achieved thus far in terms of fostering higher-wage jobs and long-term, sustainable growth and rising living standards. Trade policy will not, however, be the principal factor either in determining the different rates of growth at home and overseas, or in changing national savings and investment patterns.

It will, however, contribute to the more fundamental goals of all our economic policies: sustainable long-term growth; rising standards of living at all levels of American society; and our broader aspirations for the rule of law and strengthening international peace.

### **CONCLUSION**

As we consider the questions raised by the trade deficit, and by trade policy more

generally, the counsel of logic, and the lessons of experience, are clear. Open markets and **free** trade are of fundamental importance to America's economic and strategic interests. ..

To turn our back on open trade would be to accept a lower standard of living, loss of export opportunities, reduced rates of investment in plants and hiring, and ultimately a loss of national strength and influence worldwide.

To accept an open economy for ourselves, and to promote freer trade worldwide, is to set high standards for ourselves; to open new possibilities for our working people and industries; to reduce the cost of the essentials of life for the poor; and to accept our responsibility for world leadership.

That is the policy of the Clinton Administration, and it is one we are proud to maintain.

Thank you very much